No. 12734

United States Court of Appeals

For the Ninth Circuit

ADOLPH W. ENGSTROM, Trustee in Bankruptcy for Northwest Chemurgy Cooperative, a corporation, Bankrupt,

Appellant,

vs.

ARTHUR BENZEL

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WASHINGTON, NORTHERN DIVISION

Brief of Appellee

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Ritzville State Bank Bldg.
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APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WASHINGTON NORTHERN DIVISION

BRIEF OF APPELLEE

JURISDICTION

District Court

This is an action by a trustee in bankruptcy to recover payment of moneys alleged to be a preference and voidable under the laws of the State of Washington, Rem. Rev. Stat. § 5831-4 § 5831-6, (Complaint Tr. 3-6). Jurisdiction is conferred upon the District Court by virtue of Sec. 70 (e) (3) of the Bankruptcy Act (U. S. C. A., § 110 (e) (3).

Circuit Court

The appeal here is from a final decision of the District Court for the Eastern District of Washington, Northern Division, entered October 5, 1950 (Tr.

28-29), dismissing the action of the trustee in bankruptcy and this court is vested with jurisdiction by virtue of Title 28, U. S. Code §1291, (28 U. S. C. A., §1291).

STATUTES INVOLVED

Appellant's action is based upon Rem. Rev. Stat. of the State of Washington, being §5831-4 and §5831-6 (Laws of 1941, Chap. 103) as set forth in appellant's brief. A Preference is claimed. "Preference" is defined by sub-paragraph (c) Rem. Rev. Stat. 5831-4 as follows:

> " 'Preference' means a judgment procured or suffered against itself by an insolvent corporation or a transfer of any of the property of such corporation, the effect of the enforcement of which judgment or transfer at the time it was procured, suffered, or made, would be to enable any one of the creditors of such corporation to obtain a greater percentage of his debt than any other creditor of the same class." (L. '41, ch. 103, §1)

It is apparent from reading the statute that the language of the definition refers to payment of a pre-existing debt and was never intended to apply to a cash sale where delivery of goods and payment therefor are concurrent and mutually dependent acts, or where the check accepted in payment of such goods was dishonored on presentation.

STATEMENT OF THE CASE

The appellant and appellee each presented differ-

ent versions of the transaction in question as contained in the "Agreed Statement of Facts." In view of the conclusions of the Honorable Sam M. Driver, Judge of the United States District Court, it will be properly assumed in presenting appellee's statement of the case that the District Court adopted appellee's version of the transaction in question as follows:

On January 3, 1947, the Defendant Benzel desired to sell and Chemurgy desired to buy 1000 bushels of wheat represented by a negotiable warehouse receipt. Negotiations looking to the sale of the wheat were conducted by Mr. R. D. Whitmore on behalf of Chemurgy and Mr. Ralph Snyder on behalf of Benzel. Snyder, as agent for Benzel, had no authority to sell said wheat *except for cash* and so informed Whitmore (Tr. 13).

> "* *That Whitmore thereupon informed Snyder that the sale would be a cash sale * * and promised that the check of Northwest Chemurgy would be mailed January 3, 1947, in the sum of $1627.50, payable to Benzel, * *" (Tr. 13).

Whitmore further informed Snyder that to effect a cash sale the warehouse receipt in question must be mailed to Chemurgy the same date.

Whitmore selected the channels (via mail) through which delivery of the check and warehouse receipt were to be accomplished. Benzel resided in Ralston, Washington and Chemurgy is located in Wenatchee, Washington (Tr. 12).

That although the delivery of the warehouse receipt and the check in payment therefor were to be simultaneous acts, Chemurgy failed to mail the check on January 3, 1947. (Tr. 13).

Chemurgy's check was dated January 13, 1947, and received by Benzel January 14, 1947.

Benzel never at any time authorized Chemurgy to delay either payment or delivery of the check.

That the check was deposited by Benzel in the Ritzville Branch of the Old National Bank on January 18, 1947, presented for collection to Wenatchee Valley Branch, Seattle-First National Bank and returned "because there were no funds on deposit * * to pay said check." (Tr. 14-15).

Benzel then contacted Whitmore and Whitmore by letter dated January 22, 1947, falsely advised Benzel that the check had been returned by the bank in error and requested Benzel to re-deposit the check (Tr. 15) (Exhibit "B" Tr. 17).

Benzel re-deposited the check and the same was received by Wenatchee Valley Branch Seattle-First National Bank January 27, 1947, but was not paid for lack of funds until February 3, 1947.

Upon oral argument and briefs and based on the "Agreed Statement of Facts" the District Court found "* * that the plaintiff has failed to sustain the burden of proving that the transaction constituted an unlawful preference and was other than a cash

transaction." (Paragraph III Findings of Fact and Conclusions of Law Tr. 26).

The District Court thereupon concluded as follows:

I.

That payment of said check out of the funds of Chemurgy on deposit with the Wenatchee Valley Branch of the Seattle-First National Bank on February 7, 1947, was not such a transfer to the defendant of the property of said involvent Northwest Chemurgy Cooperative as to constitute an unlawful preference within the meaning of Rem. Rev. Stat. of the State of Washington, §5831-4, as the transaction was in substances and effect a cash transaction and there was no intent on the part of either party to create a debtor-creditor relationship.

The District Court thereafter on October 5, 1950, entered its Judgment dismissing appellant's action (Tr. 28-29).

INTRODUCTORY ARGUMENT

1. AS A MATTER OF FACT: The transaction in question was a cash sale as shown by the "Agreed Statement of Facts" (Tr. 10-16), and therefore not a "Preference" as defined by Rem. Rev. Stat. 5831-4 (c).

2. AS A MATTER OF LAW: "Where the buyer of goods pays for the same by a check, which is dis-

honored on presentation, the seller may retake the goods or recover the proceeds thereof from the trustee in bankruptcy of the buyer, Perpall (1919) 168 C. C. A. 104, 256 Fed. 758" (31 A. L. R. 586 note "e creditor of buyer").

ARGUMENT

I.

In the absence of an agreement to the contrary, it is presumed that a sale of personal property is a cash sale.

II.

Where upon a cash sale of wheat a check is accepted as means of payment, such payment is conditional only and between the immediate parties title in the buyer does not become absolute until the check is paid.

III.

Where a seller accepts payment of goods by a check dishonored on presentation, the seller may either recover the proceeds of the sale or retake the property from a trustee in bankruptcy of the buyer for the reason:

(a) Payment by check is required by commercial necessity to be a conditional payment.

(b) Title to the goods does not pass until the check is paid.

(c) General creditors have no legal or moral

right to the property so acquired as no consideration flows to seller until payment of the check.

(d) Relinquishment of seller's right to retake the property creates a present consideration for the subsequent payment of a dishonored check.

I.

In the absence of an agreement to the contrary, it is presumed that a sale of personal property is a cash sale.

The "Agreed Statement of Facts" demonstrates conclusively that a cash sale of wheat was effected by Benzel and Chemurgy. Even in the absence of the "Agreed Statement of Facts" we arrive at the same conclusion. Credit was not extended to Chemurgy, nor did Benzel extend the time in which payment was to be made to him. Delivery of the warehouse receipt representing the wheat to be sold was made through the customary channels of commerce (via mail) and at the request of Chemurgy. It was agreed the sale would be for cash. The delivery of the warehouse receipt and the check in payment therefor were concurrent and mutually dependent conditions. It is commercially impracticable, as suggested by appellant, to treat the delivery of negotiable paper and the acceptance of payment therefor by check as a credit transaction. Such is not the policy of the law nor the custom of the trade. To so hold would place an unnecessary burden on commerce and would prevent the sale of millions of bushels of wheat annually

except on overburdening escrow arrangements. Millions of bushels of wheat are sold for cash by the endorsement and delivery of negotiable warehouse receipts in exchange for checks in payment thorefor. It would be relatively impossible for any warehouseman to keep sufficient funds on hand to pay for the purchase of wheat in cash.

Washington is by statute committed to the rule that delivery of goods and payment therefor are concurrent conditions, each dependent on the other. Rem. Rev. Stat., Laws of the State of Washington, §*5836-42* is quoted as follows:

> "Delivery and payment are concurrent conditions. Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions; that is to say, the seller must be ready and willing to give possession of the goods to the buyer in exchange for the price and the buyer must be ready and willing to pay the price in exchange for possession of goods." *(L. '25, Ex. Ses., p. 372, § 42).*

Consequently, where a check is accepted as payment for personal property, payment is conditional and title to the property, *as between the parties*, does not pass until the check is paid on presentation. If such check is presented and payment is refused for want of funds the seller can elect to retake the property or recover the proceeds thereof. This proposition is fully supported and is the Washington rule as shown by subsequent cited authority.

Since Benzel and Chemurgy did not agree to give,

extend or accept credit the transaction even in the absence of the "Agreed Facts," is presumed to be a cash sale. A precise and well worded definition of the general rule appears in *Gustafson v. Equitable Loan Association*, 186 Minn. 236, 243 N. W. 106 (1932) at page 107 of the Reporter.

> "In the absence of evidence indicating that credit is to be given, a sale is presumed to be for cash. In the instant case, it was expressly stated that the sale was to be for cash."

In the case at bar, it was expressly stated by Whitmore representing Chemurgy that the sale was to be for cash.

> "Whitmore thereupon informed Snyder that the sale would be a cash sale." (Tr. 13).

The writer quotes again from page 107, *Gustafson v. Equitable Loan Association* (supra).

> "Payment and delivery in the sale of personal property are concurrent and mutually dependent acts. If the payment is evaded by the purchaser upon getting possession of the property, the seller may immediately reclaim the property; the title in such case not passing to the purchaser, the delivery being merely conditional, and the purchaser taking simply as trustee for seller until the condition is performed."

Although all facts indicate a cash sale of wheat in the ordinary course of business the transaction would not be different in the absence of the agreed facts. A cash sale is presumed. No presumption of extension of credit arises from the acceptance of a check in payment of goods, or that the check is absolute pay-

ment for the goods. On the contrary, the rule is otherwise. Again quoting from *Gustafson, supra* at page 107:

> "A check is not payment. It is only so when the cash is received on it. There is no presumption that a creditor takes a check in payment, arising from the mere fact that he accepts it from his debtor. The presumption is just the contrary. Where payment is made by check drawn by a debtor on his banker, this is merely a mode of making a cash payment, and not giving or accepting a security. Such payment is only conditional, or a means of obtaining the money. In one sense the holder of the check becomes the agent of the drawer to collect the money on it; and if it is dishonored there is no accord and satisfaction of the debt. * * Where goods are sold for cash on delivery and payment is made by the purchaser by check on his banker, such payment is only conditional, and the delivery of the goods also only conditional; and if the check on due presentation is dishonored, the vendor may retake the goods." (Cited cases omitted). "It follows that the title never passed from plaintiff to Madden."

II.

Where upon a cash sale of wheat a check is accepted as means of payment, such payment is conditional only and between the immediate parties title in the buyer does not become absolute until the check is paid.

The proposition of law above is not only controlling in the case at bar, but is the Washington rule and is adhered to by Federal Courts and courts generally:

In *Quality Shingle Co. v. Old Oregon Lumber & Shingle Co.*, 110 Wash. 60, 187 Pac. 705, the Wash-

ington Supreme Court had before it a case in which the seller delivered a non-negotiable bill of lading for shingles upon receiving a check for the purchase price. The check was subsequently dishonored for lack of funds. Even though the rights of a third party had intervened, the court held at page 63 of the Washington Report:

> "That the sale agreement entered into between respondent and the Shepard-Traill Company was an agreement for a cash sale, that Shepard-Traill Company obtained possession of the bill of lading by giving its check for the agreed purchase price to respondent and by representing to the respondent that the check would be paid upon presentation, that respondent took the check believing in good faith that it was in fact being paid for the shingles in cash, and that the check was promptly in due course presented for payment which payment was refused, we think is quite clear.
>
> "It seems to us to follow, in the light of elementary rules of law, that, as between respondent and Shepard-Traill Company, the title to the shingles did not pass from respondent to Shepard-Traill Company upon it receiving the bill of lading for the shingles and giving its check to respondent therefor."

The same result was reached in *Standard Investment Co. v. Town of Snow Hill, N. C.*, 78 Fed. (2d) 33, where a negotiable bond was sold and the check in payment therefor dishonored on presentation as shown by the language of the Fourth Circuit Court appearing at page 35 as follows:

> "P. 35. There can be no question, we think but that the title of the bank was defective. The

> sale was a cash transaction, in which the passage of title depended on payment; and it is well settled that, in absence of special agreement to the contrary, a check is conditional payment only and does not operate to effect payment unless it is itself paid (Citing Federal cases here omitted). The rule that a check of the debtor is merely conditional payment applies to obligations arising out of immediate transactions, as well as to payment of antecedent debts; and, where there is a sale for cash on delivery, and payment is made by check of the buyer, such constitutes only conditional payment. Until the check is itself paid, the title, as between the parties, passes only conditionally; and, upon dishonor of the check, the seller may rescind the transaction and reclaim that with which he has parted." (Citing Federal cases here omitted).

That the proposition for which appellee contends is not only the Washington and Federal rule but the rule adopted by courts generally, see *(J. W. Young v. Harris Cortner Company et al*, 152 Tenn. 15, 268 S. W. 125, 54 A. L. R. 516, and Anno. 54 A. L. R. 526). (See also Anno. 31 A. L. R. 578-581) (46 Am. Jur. "Sales" Sec. 564 p. 708).

In contradistinction to appellant's position, it is noted that Mr. Williston on Sales also recognizes this rule. See the Young case *(supra)* at pages 518-519 (pages reference to A. L. R.)

> "Upon principle we are unable to distinguish the instant cause from that of a sale made over a counter where the seller was induced to accept a check as cash. Such transactions are treated by the authorities as conditional sales, the title not passing until the condition (the payment of the check) is complied with, or, as stated by Mr.

Williston, the purchaser only has a contract right until the price is paid."

(In the Young case, *supra*, the cotton sold was represented by a negotiable warehouse receipt and Tennessee has adopted the Uniform Sales and Negotiable Warehouse Receipts Acts).

III.

Where a seller accepts payment of goods by a check dishonored on presentation, the seller may either recover the proceeds of the sale or retake the property from a trustee in bankruptcy of the buyer for the reason:

(a) Payment by check is required by commercial necessity to be a conditional payment.

(b) Title to the goods does not pass until the check is paid.

(c) General creditors have no legal or moral right to the property so acquired as no consideration flows to seller until payment of the check.

(d) Relinquishment of seller's right to retake the property creates a present consideration for the subsequent payment of a dishonored check.

The rule above as contended for by appellee has so long been the rule adopted by Federal Courts that the proposition for many years has not been seriously disputed.

The rule is adhered to and followed by the Federal Court in the following cases:

In Re A. O. Brown & Co., 189 Fed. 442.

In Re Perpall, 256 Fed. 758.

Marion Mach. Foundry v. Giraud, 285 Fed. 160.

Hough v. Atchison T. & S. F. Ry. Co., 34 Fed. (2d) 238.

In Re Z. J. Fort-Tidwell Co., 34 Fed. (2d) 238

In each of the above cited cases the check received as payment was dishonored on presentation (Note sight draft in *Hough case* treated as worthless check).

The writer will quote at length from the *Hough case, supra,* but will first adopt the language of the annotator appearing in 31 A. L. R. 586,

> "Where the buyer of goods pays for the same by check, which is not paid, the seller may retake the goods or recover the proceeds thereof from the trustee in bankruptcy. *Re Perpall* (1919) 168 C. C. A. 104, 256 Fed. 758."
>
> "As between the trustee in bankruptcy of the buyer and the seller, actual fraud in inducing the seller to deliver the goods need not be shown; it is sufficient in this regard if the sale was made upon condition, which was never performed. The fact that the seller accepted a check which was never paid does not affect his right to claim goods delivered under the belief that the check would be paid, although given in payment of other goods, payment being a condition to delivery. *Marion Mach. Foundary & Supply Co. v. Giraud* (1922) 285 Fed. 160."

In the *Hough case, supra,* the court treated the sight drafts as worthless checks. The court at page 240 recognizes the fact that checks are the usual method of consummating cash transactions of this kind and points out that the "preference" must be at the expense of the other creditors before it is voidable.

> "Again, the Bankrupt Law undertakes to prevent one creditor from obtaining a preference at the *expense* of other creditors in like situation. 'Cash transactions are not within the prohibition.' *Remington on Bankruptcy* (3d Ed.) Sec. 1695. The use of checks or their equivalent

is the accepted method of consummating cash transactions of this size."

Continuing in the language of the Court:

> "*In re Perpall*, 256 F. 758. And in another case of the same title (271 F. 466) the same court declined to require a *creditor* to pay back to the trustee the proceeds of a check which he had received for the purchase price of bonds, notwithstanding the fact that the check was received and paid after the filing of the petition in bankruptcy, and notwithstanding the fact that some hours elapsed between the delivery of the bonds and the receipt of the check. It was held that the entire matter was a cash transaction, notwithstanding the use of checks instead of currency, and notwithstanding the lapse of a short period of time between the delivery of the bonds and the receipt of the check."

In referring to *Illinois Parlor Frame Co. v. Goldman*, 257 Fed. 300 (7 C. C. A.) where the right to rescind a contract of sale arose out of a fraudulent sale, the Tenth Circuit Court speaking in the *Hough case, supra*, said:

> "But on June 9th appellant concededly had a right to rescind the fraudulent sales and to recover back such of the goods as were then in the bankrupt's possession. Clearly a return of these goods would not be a preference; to the extent of their value, payment could no more effectuate a preference; neither transaction would diminish the estate to which the bankrupt was entitled. That appellant did not expressly assert a right of rescission is immaterial; it relinquished that right in confirming the sale; it then gave up a property interest equal to the value of the goods then on hand. To that extent the transfer was for a present consideration, and not preferential."

Just as clearly the return of the warehouse receipt or the payment of the check delivered to Benzel could not work a preference as Chemurgy's estate would not be diminished thereby.

The court in the *Hough case* held that a preference does not arise where seller recovered goods obtained by giving a worthless check.

> "*Mulroney Mfg. Co. v. Weeks*, 185 Iowa, 714, 171 N. W. 36, it was held that where a bankrupt secured possession of goods by giving a worthless check, the recovery of the goods does not constitute a preference. To the same general effect, see Manly v. Ohio Shoe Co., (4 C. C. A) 25 F. (2d) 384, 59 A. L. R. 413, In re Weissman (2 C. A. A.) 19 F. (2d) 769, 51 A. L. R. 644 * *"

The general creditors of Chemurgy were not injured in any way by the payment of the check in question. The relative rights of the parties is clearly expressed in the language of the *Hough case, supra.*

> "In the case at bar, the possession of the freight was procured by the giving of sight drafts which were dishonored on presentation. The railway company had a right to recover the possession so wrongfully obtained. Such recovery would not have diminished the estate to which the creditors are rightfully entitled, nor constitute a preference. Accepting payment of the draft, in lieu of recovery of the goods, is not a recoverable preference. From whatever angle you may look at it, one fact stands out: The bankrupt procured possession of this crate material by giving the equivalent of worthless check. The creditors have no legal or moral right to the crate material, or its sale price, without paying the freight."

From whatever angle we view the transaction in question Chemurgy gained possession of the warehouse receipt by giving a worthless check therefor and the creditors have no moral or legal right to retain the wheat without paying therefor.

It is unconscionable that the trustee attempts to gain a benefit growing out of the giving of a worthless check and the fraudulent acts of the buyer.

The balance of this brief will be devoted to answering appellant and summary.

It is not difficult for appellant to make a plausible argument based on the implausible conclusion that the sale in question was a sale on credit.

Appellant does not cite one case in which the trustee in bankruptcy was permitted to retain property procured by issuance of a worthless check; nor does appellant submit one case in which the trustee was permitted to recover the proceeds of a dishonored check from a seller and yet retain the seller's property.

It is significant that in all cases cited by the appellant, the sale was either a sale on credit or the check was given in payment of an antecedent debt.

In *Seattle Assn. of Credit Men as Assignee v. P. D. Luster*, 137 Wash. Dec. 181 (1950) 222 Pac. (2d) 843 cited by appellant as the cornerstone of his argument was an action in which credit was extended by the

seller to the buyer as shown at page 182 (Wash. Dec.):

> "The buyer informed seller in writing: 'We are also submitting our check for the balance *with the distinct understanding that this check is to be held until the customer has paid for this shipment in full.*'"

The checks of the buyer could not be presented for payment by the seller until the subpurchaser had paid buyer in full.

The language of the cited case, referring to *Stern v. Lone*, 32 Wn. (2d) 785, 203 Pac. (2d) 1074, explodes appellant's theory, however, to the effect that the mere cashing of a check within the four-month prohibitionary period works a preference.

> "But this is only true, of course, if the checks are cashed in payment of an antecedent debt. Before a preference may arise, a transfer of *debtor's property* must result in a diminution of the estate available for his other creditors."

The writer has no quarrel with the result arrived at in *Seattle Assn. of Credit Men, supra.* The seller there by voluntary agreement extended the time of payment and thus extended credit to the buyer. More than that, however, the seller could not claim payment until the property was sold to a subpurchaser and then only after the proceeds of such sale to the subpurchaser had been paid over to the account of the buyer. Under the facts no other result should obtain.

Seattle Assn. of Credit Men v. Daniels, 15 Wn. (2d) 393, 130 Pac. (2d) 892, cited by appellant, was not a sales contract, but one for work and service in which credit was extended. The claimant could not demand payment nor was payment required to be made until receipted bills and payroll had been presented, audited and ordered paid. Under the facts there was an extension of credit and payment of a pre-existing indebtedness.

In *Stern v. Lone*, 32 Wn. (2d) 785, 203 P. (2d) 1074, cited by appellant neither party claimed the transaction was a cash sale.

In *Seattle Assn. of Credit Men v. Hudson Mach. Co.*, 135 Wash. Dec. 643 (1950) 214 Pac. (2d) 681, there was a voluntary extension of credit. Seller was one of a number of general unsecured creditors who had extended credit to the insolvent. That the seller was an unsecured creditor is admitted. "Respondent acknowledges that it is an unsecured creditor."

Although appellant argues to the contrary, the warehouse receipt in question, as between the original parties was nothing more than a simple contract in writing and subject to all the defenses both at law and equity existing in the original parties. (See *Vancouver National Bank v. Katz*, 142 Wash. 306, 252 Pac. 934).

Neither was Chemurgy a holder in due course and

a negotiable instrument is subject to same defenses as if it were non-negotiable in the hands of a holder other than a holder in due course *(Rem. Rev. Stat. of Wash.* § 3449). Lack of consideration is a matter of defense *(Rem. Rev. Stat. of Wash.* § 3419) and as between the parties it may be shown that delivery was conditional *(Rem. Rev. Stat. of Wash.* § 3407).

As has been previously demonstrated the courts hold that the acceptance of a check is merely a conditional payment and that in cash sales the delivery of goods and the payment therefor are concurrent and mutually dependent conditions. Any argument to the contrary suggests that Chemurgy can gain greater rights out of the issuance of a worthless check than one paid on presentation for it is admitted by appellant that no preference would be claimed had the check been paid on presentation. Chemurgy, by the acts of its agents, cannot make Benzel its involuntary creditor by issuing him worthless paper.

SUMMARY

The facts reveal that Snyder representing Benzel and Whitmore representing Chemurgy entered into an agreement for the cash sale of wheat. Snyder had no authority to sell the wheat except for cash. The delivery of the wheat receipts and the check in payment thereof were concurrent and mutually dependent acts. The sale was made in the ordinary

course of business and the checks and receipts delivered through channels selected by the buyer. The check was accepted as means of payment and title to the wheat did not become absolute in the buyer until the check was paid. Benzel had the right upon dishonor of the check to retake the property or to recover the proceeds of the sale. Benzel elected to recover the proceeds of the sale rather than retake the property. The waiver of the right to Benzel to retake the property is a sufficient present consideration passing to the creditors for the recovery of the proceeds of the sale. That the creditors have no moral or legal right to obtain something for nothing and that in such case Benzel could recover from the trustee in bankruptcy if he did not already have possession of the proceeds of the sale.

Appellee submits that under both the law and the facts that the judgment of the District Court should be affirmed.

Respectfully submitted,

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Attorney for Appellee